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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of

Review of the Commission's
Regulations Governing Programming
Practices of Broadcast Television
Networks and Affiliates

)
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) MM Docket No. 95-92
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DOCKET FILE COPY ORIGINAL

COMMENTS OF CBS INC.

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SUMMARY

CBS Inc. strongly supports the Commission's decision to comprehensively reevaluate its network-affiliate rules in light of the fundamental changes that have taken place in the video marketplace since the rules were adopted some fifty years ago. Those changes and the highly competitive conditions that now prevail in the television industry demonstrate convincingly that the rules under consideration in this proceeding -- the right to reject rule, the time option rule, the exclusive affiliation rule, the dual network rule and the network territorial exclusivity rule -- may be eliminated or substantially modified without compromising the Commission's goals of fostering the development of new networks and ensuring licensees' ability to fulfill their public interest obligations. In fact, deregulation of these aspects of network-affiliate relations is necessary to promote the continued viability of universal, free network broadcasting and will encourage rather than hinder the development of competition in the television industry.

In 1977, the Commission eliminated most of the network-affiliate rules for radio, reasoning that with the sharp reduction of "network dominance" resulting from changes in the industry, the potential abuses the rules were intended to prevent were unlikely to develop. Today, 15 years after the Commission's Network Inquiry Staff called for the elimination of these rules as to television as well, there can be little doubt that the concept of "network dominance" on which the rules were premised is an anachronism.

Since 1970, the number of television stations not affiliated with the three original networks has increased from 82 to over 450. Three new broadcast networks have been created, including one that is a full-fledged competitor of the original three, and the Commission has concluded that the number of independent stations remains large enough to allow new networks to

add affiliates and expand audience reach. There has also been dramatic growth in cable networks, which have become major purchasers of television programming. In addition, other multichannel program distributors, most notably direct-to-home satellite services, are on the rise. In this environment, it is clear that the three original networks cannot inhibit the development of competitors through undue control over the available outlets for television programming. Accordingly, regulatory restrictions on clearance provisions in network-affiliate agreements are unnecessary to allow competing program distributors to grow and prosper.

Nor are such regulations necessary to ensure that licensees retain sufficient control over their stations to fulfill their public interest obligations. It is far from clear that networks have ever had the power, through pressure for clearance of their programs, to overwhelm the preferences of affiliates to present other programs instead. There is even less reason for concern today that, in the absence of regulation, affiliates' program choices will be somehow dictated by their network partners. Thus the growth of new networks, and the vastly increased supply of first-quality original syndicated programming, have greatly increased the bargaining power of affiliates with respect to their networks.

At the same time, the three networks are under increasing competitive pressure. The audience shares of the three original networks have dropped precipitously both in prime time and other dayparts. The networks have also suffered a significant decline in their shares of national advertising revenues. In light of these trends, if the networks are to compete effectively as distributors of first-quality programming against dual revenue stream providers, they must be permitted to maximize the efficiency of their distribution. Regulations that artificially reduce the

networks' ability to bargain for clearance of their programs undermine the viability of universal, over-the-air broadcasting, and promote the shift of quality programming from free television to cable.

Against the background of these developments in the industry, there is a compelling case for elimination or substantial modification of most of the network-affiliate rules, particularly those limiting networks' ability to bargain for greater program clearances. We therefore support, with certain qualifications, the Commission's specific proposals.

CBS strongly supports the Commission's proposal to retain the right to reject rule, while clarifying that it may not be invoked solely for economic reasons. While affiliates should be allowed to preempt network programming based on public interest considerations, they should not receive governmental protection for preemptions made primarily for reasons of financial gain. The Commission's proposed clarification of the rule, however, would be significantly undermined by the Notice's suggestion that the rule would still permit stations to preempt network programming to air local sporting events or local entertainment programs. Since by far the largest category of preemptions of prime time CBS programs -- over 40 percent -- is accounted for by affiliates' coverage of sporting events, exempting sports coverage from the proposed clarification would greatly reduce its intended effect. We submit that once a station has made the economic decision to be a network affiliate and to enjoy the economic benefits of affiliation, it should not be entitled to a governmentally-guaranteed right to act in its own economic interest -- and to the detriment of the network system of which it is part -- simply because a sports event in which it seeks to sell commercial availabilities is "local."

CBS agrees with the Commission that the prohibition on time optioning should be relaxed, but believes that a total repeal of the rule is warranted. Like the Commission, we question whether the practice of time optioning ever resulted in the feared consequences that led to promulgation of the rule. CBS therefore supports the Commission's proposal to allow time optioning arrangements. We do not believe, however, that such arrangements should be subject to a governmentally-determined notice period of the network's intent to program an optioned time period. Rather, notice provisions should be left to individualized marketplace negotiations between the affected parties.

CBS also supports the Commission's proposal to eliminate the prohibition on exclusive affiliations, and urges that the regulation be repealed as to all markets, not only large ones. Today, 69 percent of U.S. television households are in DMAs with six or more commercial television stations, and cable penetration in markets with fewer than six commercial stations is on average 66 percent. In this environment, ample opportunities exist for new networks to find outlets for their programming. Moreover, in small markets with relatively few broadcast stations, those stations will have significant bargaining power to retain the right to take programming from other networks if it they wish to do so.

CBS submits that the dual network rule should also be repealed. We believe the rule is unnecessary for the protection of new networks, places networks at a competitive disadvantage in relation to nonbroadcast multiple channel providers, and will impede advances made possible by digital compression.

We are also in agreement with the Commission's proposals with respect to the network territorial exclusivity rule. CBS supports repeal of the first prong of this rule, which prohibits agreements granting an affiliate exclusivity as to non-cleared network programs within its own community of license. Since alternate clearances are in practice rare, elimination of the rule would have a negligible effect on the viewing public, while allowing affiliates to strengthen their network brand identities. However, we agree with the Commission that repeal of the second prong of the territorial exclusivity rule, which prohibits stations from preventing their networks from affiliating with a station in a different community of license, would confer no efficiency benefits and could have significant costs in terms of lost access to network programming.

Finally, CBS submits that the cumulative effect of the proposals advanced in the Notice and in these comments would not have an undue impact on the ability of local stations to control their own program choices or on the development of new networks. To the contrary, adoption of these measures would allow established and new networks to compete more effectively in the current competitive video marketplace, without lessening the ability of affiliated stations to fulfill their public interest obligations.

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COMMENTS OF CBS INC.

CBS Inc. ("CBS") hereby respectfully submits its comments in response to the Commission's Notice of Proposed Rule Making ("Notice") in the above docket, in which the Commission continues its reexamination of the rules which regulate the relationship of television networks and their affiliates.

The rules at issue in this proceeding -- the right to reject rule, the time option rule, the exclusive affiliation rule, the dual network rule, and the network territorial exclusivity rule -- were first adopted more than half a century ago. Like the recently repealed financial interest/syndication rules and the prime time access rule which the Commission has scheduled for elimination in August 1996, most of these regulations are premised on a theory of "network dominance" which has no viability in today's video marketplace. CBS therefore strongly endorses the Notice's call for a "comprehensive review" of the network-affiliate rules in light of the competitive conditions which now prevail in the television industry. That review, we submit, will convincingly demonstrate that the rules may be eliminated or substantially modified without any adverse impact on the public interest.

In Section I of these comments, we discuss the changes in the competitive environment faced by television networks which have made the concerns on which most of the rules are based obsolete, and the ways in which the rules hamper the ability of over-the-air networks to compete with their growing array of rivals offering multichannel subscription services. We comment in Section II on the specific proposals for repeal or modification of the rules set forth by the Commission in the Notice, and in Section III on the cumulative effect of the proposals we believe should be adopted.

I. Introduction and Overview.

The Commission's network/affiliate rules were adopted as to radio in the Commission's 1941 Report on Chain Broadcasting,¹ and extended to television in 1946.² They were premised on the belief that "the major...networks' power over their affiliates was impeding the development of new program sources and impairing the affiliated stations' ability to control their day-to-day operations."³ Most of the rules adopted in the Report on Chain Broadcasting were therefore directed, in substance if not in form, to network behavior.⁴

¹ Report on Chain Broadcasting, Commission Order No. 37, Docket No. 5060 (May 1941), modified, Supplemental Report on Chain Broadcasting (October 1941), appeal dismissed sub nom. NBC v. United States, 47 F. Supp. 940 (S.D.N.Y. 1942), aff'd, 319 U.S. 190 (1943) ("Chain Broadcasting Report").

² Notice at ¶2, citing Amendment of Part 3 of the Commission's Rules, 11 Fed. Reg. 33 (Jan. 1, 1946)

³ Notice at ¶2.

⁴ The peculiar form of the network/affiliate rules -- which state that "no license shall be granted to a television broadcast station" entering into an affiliation agreement containing specified provisions, rather than simply prohibiting a network from imposing such terms, see e.g., 47 C.F.R. §73.658(a) -- is in most cases attributable to
(continued...)

The right to reject and time option rules limited the ability of networks contractually to bargain for clearance of their programs, reflecting the Commission's belief that such provisions "place[d] a serious obstacle in the way of the development of new networks"⁵ and also "hamper[ed] the efforts of the [affiliated] station to develop local commercial programs."⁶ The exclusive affiliation rule prohibited any network affiliation agreement which prevented the affiliate from broadcasting programs offered by another network, in order that potential new network entrants would not be stifled by the lack of available outlets for their programming, and affiliates would not be "denied freedom to choose the programs which they believe best suited to their needs."⁷ Finally, the dual network rule prohibited a single entity from simultaneously operating more than one network in the same territory, a practice which was also thought detrimental to the development of competition from new network sources.⁸

In June 1977, the Commission reviewed the network-affiliate rules as they applied to radio networking. The Commission concluded that, in view of the sweeping changes which had occurred in the radio industry, most of the rules were no longer necessary

⁴(...continued)

the Commission's clear jurisdiction over the licensing of stations and its less certain jurisdiction over networks. However, the network territorial exclusivity rule, unlike the others, actually is directed toward contractual provisions likely to be sought by affiliates, and which have been perceived to be contrary to the public interest.

⁵ Chain Broadcasting Report at 63-64.

⁶ Id. at 63.

⁷ Id. at 52.

⁸ Id. at 72.

simply because (under these vastly different circumstances and with sharply reduced "network dominance") the abuses and practices dealt with are unlikely to develop to any substantial extent.⁹

Three years later, the Commission's Network Inquiry Staff concluded that the rules governing network-affiliate relations were as ill-suited to the current state of television as the Commission had found them to be with respect to radio. Accordingly, the staff recommended abolition of the right to reject, time option, and exclusive affiliation rules,¹⁰ and advocated easing of the limitations on dual networking.¹¹

Today, more than half a century after the original adoption of the network-affiliate rules, and 15 years after the Network Inquiry Staff called for their elimination as to television, there can be no serious doubt that the concept of "network dominance" underlying the regulations is an anachronism. As in the case of radio, momentous changes in the competitive environment in which television networks operate have made the supposed abuses which concerned the Commission in 1941 not only unlikely to occur, but remote in the extreme. These marketplace

⁹ Network Broadcasting by Standard (AM) and FM Broadcast Stations, 63 FCC 2d 674, 679 (1977) ("Radio Deregulation"). While abolishing the rules that had prohibited the networks from imposing requirements on licensees, the Commission retained its rule prohibiting networks from granting territorial exclusivity to their affiliates.

¹⁰ Network Inquiry Special Staff, New Television Networks: Entry, Jurisdiction, Ownership and Regulation, Final Report (Oct. 1980) at 475-91 ("Network Inquiry Report").

¹¹ See id. at 366-72.

changes have been extensively documented by the Commission in a series of orders and reports,¹² and need only be briefly summarized here.

Since 1970, there has been a dramatic increase in the number of television stations not affiliated with the three original networks. The Commission recently found that the number of commercial independent stations has grown from 82 in 1970, to over 450 in February 1994.¹³ By the Commission's reckoning, there were 278 independent stations in the top 50 markets in 1994, for an average of 5.6 per market.¹⁴ The Commission has also found that "in 1993, 70 percent of all television households received 11 or more over-the-air channels."¹⁵ In the same year, the average television household could receive 13.3 stations.¹⁶

In only eight years, the Fox Network has emerged as a full-fledged competitor to ABC, CBS and NBC, and two new networks, both affiliated with powerful and deep-pocketed Hollywood studios, began service during 1995. A seventh network, to be built around the nucleus

¹² See, e.g., Report and Order In re Review of the Prime Time Access Rule, MM Docket No. 94-123 (released July 31, 1995) ("PTAR Report and Order"); Second Report and Order in MM Docket No 90-162, 8 FCC Rcd 3282, recon. granted on other grounds, 8 FCC Rcd 8270 (1993) ("Fin/Syn Second Report and Order"); Setzer and Levy, Broadcast Television in a Multichannel Marketplace, OPP Working Paper No. 26, 6 FCC Rcd 3996 (1991) ("OPP Report").

¹³ PTAR Report and Order at ¶27. See also An Economic Analysis of the Prime Time Access Rule, at 9-10, Economists Incorporated (March 7, 1995), submitted on behalf of ABC, CBS and NBC in MM Docket No. 94-123 ("PTAR Joint Economic Study").

¹⁴ PTAR Report and Order at ¶27.

¹⁵ Notice of Proposed Rulemaking in MM Docket No. 94-123, FCC 94-266 (released October 25, 1994) at ¶16 ("PTAR Notice"), citing Nielsen Media Research, Television Audience 1993, at 9.

¹⁶ PTAR Joint Economic Study at 59.

of the 12 stations owned by Silver King Communications, is apparently in the offing.¹⁷ As of July 1995, it was the Commission's view that "the numbers of independent stations remain large enough to make it possible for new networks to add affiliates and expand audience reach."¹⁸

An explosion in the number of cable subscribers has been accompanied by a similarly dramatic growth in the number of cable networks, which have become major purchasers of original television programming.¹⁹ First-run syndication has also experienced extraordinary growth, with the number of first-run programs sold increasing from 45 in 1970 to 250 in 1990.²⁰ By

¹⁷ Barry Diller, the new chairman and chief executive of Silver King, who was instrumental in the development of the Fox network, reportedly plans to create a network from the nucleus of the company's 12 UHF stations, which reach 28 million homes. Silver King apparently will rely on its right to cable carriage of its UHF signals, and possible deals with cable operators outside the markets in which it has stations, to expand its audience. See "Diller, As Expected, Is Named Chief Of Silver King," The New York Times, August 26, 1995 at 33, 37.

The approach contemplated by Silver King is not unique. The WB Network has combined over-the-air broadcast signals, must carry rights and agreements with cable companies to create a national distribution system, see, e.g., Broadcasting and Cable, Jan. 2, 1995, at 36, as has Fox. The actions of these companies demonstrate there are viable opportunities to build new networks to effectively compete with the traditional networks.

¹⁸ PTAR Report and Order at ¶101.

¹⁹ Fin/Syn Second Report and Order, 8 FCC Rcd at 3306-07. ABC, CBS and NBC combined accounted for only 30.5 percent of the first-run television series, specials, mini-series and made-for-television movies appearing on broadcast or cable television in 1994. Video entertainment programming purchased by ABC, CBS and NBC each on average accounted for only 9.4 percent of aggregate expenditures on video programming, while programming produced in-house by the three networks combined amounted to only 5.7 percent of aggregated expenditures. See PTAR Joint Economic Study at 25.

²⁰ PTAR Notice at ¶19.

1994, more than half of the most popular syndicated programs were first-run,²¹ and included original series of "network quality."²² Reflecting the reliance of independent stations on syndicated programming, the Commission recently found that "among non-Fox independent stations in the top-50 markets, 39 percent of prime time hours were first-run syndication."²³

The explosion in demand for video programming which has been occasioned by the extraordinary growth in both broadcast and non-broadcast distribution outlets can only be expected to increase. Accompanying the rise of cable television, the penetration rates of other multichannel distribution services, such as MMDS and SMATV, have also significantly risen.²⁴ Particularly notable is the remarkable early growth of direct-to-home satellite distribution services; industry sources estimate that DBS subscribers will exceed one million in 1995 and may exceed 10 million by 2000.²⁵ And waiting in the wings to provide video services directly to their customers are the regional telephone companies, whose ability to compete in the television program production, acquisition and distribution marketplaces will be formidable, whatever the legislative or regulatory ground rules to which they are ultimately subject.

In sum, if it once might have been thought that the original three networks could inhibit the development of potential competitors through undue control over the available outlets for television programming, any such fear must now be seen as the sheerest fantasy. In a competitive environment marked by the presence of over 450 television stations not affiliated

²¹ PTAR Joint Economic Study at 17-18.

²² Fin/Syn Second Report and Order at ¶ 46.

²³ PTAR Report and Order at ¶91, citing PTAR Joint Economic Study at 49-50.

²⁴ PTAR Joint Economic Study at 12-13, 70.

²⁵ Id. at 12, citing Cablevision, November 14, 1994, at 6.

with one of the three original networks, the emergence of a fourth network as a full competitor of the original three, the appearance of two "emerging" networks affiliated with major Hollywood studios, the likely entry of another new network, the growth of cable as a voracious consumer of video programming, and the presence on the horizon of DBS and the telcos, restrictions on clearance provisions in network-affiliate agreements are hardly necessary to allow competing program distributors to grow and prosper.

Nor are such regulations necessary to accomplish the second principal objective of the network-affiliate rules, i.e., "to ensure that licensees retain sufficient control over their stations to fulfill their obligation to operate in the public interest."²⁶ It is, first of all, far from clear that networks have ever had the power, through pressure for clearance of their programs, to overwhelm the preferences of affiliates to present other programming instead. In this regard, it is notable that, in the aggregate, the total programming offered by ABC, CBS and NBC has declined by 25 hours per week, from a total of 278.5 hours in 1977 to 253.5 hours in 1994.²⁷ This decrease reflects the abandonment of time periods by the networks because of low affiliate clearance rates, which demonstrates both affiliates' willingness and their ability to reject network programming in favor of alternative local or syndicated programming.²⁸

²⁶ Notice at ¶6.

²⁷ PTAR Joint Economic Study at 23, 90-91.

²⁸ CBS's experience in this regard is exemplary. In September 1993, CBS ceased supplying programming to its affiliates between 10 and 11 AM. CBS's abandonment of this time period was caused by the unwillingness of a sufficient number of affiliates to clear the programming being offered. The percentage of national household coverage by affiliates clearing the 10-10:30 AM portion of the hour decreased from 90 percent in 1986 to 49 percent at the time the decision was made to abandon the hour. National coverage for 10:30 to 11 AM decreased from 84 percent (continued...)

There is even less reason for concern today that, in the absence of regulation, programming choices by affiliated stations will be somehow "dictated" by their network partners. With the emergence of the Fox Network, which has produced intense competition among networks for affiliations in many markets, the bargaining power between networks and their affiliates has shifted dramatically.²⁹ This competition has in turn yielded numerous network-affiliate realignments; difficult and protracted negotiations by all networks to retain existing affiliates or replace those that have been lost; and significant increases in

²⁸(...continued)

to 61 percent over the same period. See Nielsen Television Index. A similar problem of non-clearance caused the abandonment of the 4-4:30 PM time period in September 1986, after national coverage had declined to 26 percent. Id.

More recently, affiliates serving more than 40 percent of national television households insisted on delaying the broadcast of THE LATE, LATE SHOW WITH TOM SNYDER, when CBS began offering the program to its affiliates in January 1995. Currently affiliates serving 34 percent of households still broadcast the program on a delayed basis. Although the total national household coverage on a live or delayed basis is gradually increasing, and is now about 96 percent, see Nielsen Television Index, the difficulty of the network in obtaining live coverage -- notwithstanding the popular success of the broadcast in those markets in which it has been carried on a live basis -- belies any notion of undue network power over affiliates' scheduling and programming decisions.

²⁹

As part of the agreement between Fox Television Stations and New World Communications Group announced in May 1994, New World agreed to change the affiliations of 12 stations it owned or was to acquire from one of the three original networks to Fox. By CBS's count, the Fox/New World deal has generated to date, directly or indirectly, 80 changes of network affiliations in 40 markets. As a result of this series of realignments, the three original networks reportedly will now pay at least \$200 million in additional compensation to their affiliate bodies. Broadcasting & Cable, "CBS's Tony Malara: In the Storm of the Eye," December 19, 1994 at 34. The Fox/New World transaction and its aftermath are discussed, inter alia, in the Comments of CBS Inc., In Re Review of the Prime Time Access Rule, MM Docket No. 94-123 (March 7, 1995) ("CBS PTAR Comments") at 18-20; and in the Comments of CBS Inc., In Re Review of the Syndication and Financial Interest Rules, MM Docket No. 95-39 at 10-12.

compensation.³⁰ In addition, the dramatic increase in the availability to television stations of original syndicated programming, as well as high quality programming from the new United Paramount and WB Networks, has clearly lessened any undue dependence which affiliates of the three original networks may once have been thought to have had on those entities.³¹

³⁰ Indeed, networks are not only paying additional compensation to preserve or obtain affiliations, they are even agreeing to carry on their owned stations syndicated programs to be developed by affiliates' production entities. See, e.g., "Company Town; NBC and New World Strike Deal," Los Angeles Times at D4 (July 11, 1995) ("In an agreement that demonstrates the shifting balance of power between television networks and their affiliates, NBC...agreed to carry programming developed by New World Communications Group on the six stations it owns in exchange for an ownership interest in the shows and renewal of affiliations with two New World Stations. ... For NBC, the arrangement helped secure affiliations in Birmingham, Ala., and San Diego, markets that it viewed as vulnerable.")

³¹ The Commission has found that:

network affiliates are in many cases preempting network programs in order to obtain new first-run product. The record supports the conclusion that first-run is a fully comparable alternative to network distribution.

Fin/Syn Second Report and Order at ¶47. Similarly, in its recent decision to repeal the secondary affiliation rule, the Commission emphasized the increased availability of programming from sources other than ABC, CBS or NBC. Thus the Commission noted that:

[i]n markets where the rule would apply today, we believe that independent stations, either UHF or VHF, should remain viable entities by looking to these alternative program sources -- including Fox, United Paramount and Warner Brothers -- even if they lose the benefit of a regulatory 'right of first refusal' on some programming of the three traditional networks. In addition, independent stations have access to a plethora of syndicated first-run and off-network programming.

Review of the Commission's Regulations Governing Television Broadcasting, 10 FCC Rcd 4538, 4542 (1995) ("Secondary Affiliation Report and Order").

The growth and profitability of independent stations underlines the viability of alternatives to network affiliation.³² Just this summer in its Report and Order repealing the prime time access rule ("PTAR"), the Commission concluded that independent stations are "on average, profitable."³³ It attributed the fact that independent television has "grown and prospered" to "advances in television design, the growth of cable penetration, and the growth in demand for television advertising," as well as the availability of "a robust supply of programming to turn to under today's market conditions."³⁴ The Commission found nothing, including the repeal of PTAR, likely to "threaten these advancements."³⁵ Independent stations are profitable not only in their own right³⁶ but also as compared to network affiliates.³⁷ In short,

³² See discussion at pp. 5-6, *supra*. See also Secondary Affiliation Report and Order, 10 FCC Rcd at 4542, where the Commission noted that, "[a]n overview of the marketplace reveals that independent UHF stations have become more competitive despite their lack of affiliation with the traditional networks, and that they no longer appear to need regulatory assistance to attract affiliations of nascent networks."

³³ PTAR Report and Order at ¶83.

³⁴ Id. at ¶70.

³⁵ Id.

³⁶ Average profits for UHF independents in 1993 were \$1.5 million. Secondary Affiliation Report and Order, 10 FCC Rcd at 4542.

³⁷ VHF independents have an average cash flow significantly higher than that of the average network affiliate. See PTAR Joint Economic Study at 53-54, Figure 17, and Appendix A, Table A-12. UHF independents have an average cash flow of over \$2 million, significantly higher than that of network UHF affiliates. Id. at 54-55, Figure 18, and Appendix A, Table A-16. While these comparisons reflect the fact that VHF and UHF independents are in larger markets, respectively, than are the average network affiliate and UHF network affiliates, the fact remains that both VHF and UHF independents are "growing and prospering" and should continue to do so.

network affiliation has become but one option among many available to the nation's television stations.³⁸

At the same time that these changes have lessened program producers' dependence on networks, increased programming alternatives for network affiliates and independents, and provided new outlets for emerging networks, the three original networks themselves have faced ever increasing competitive pressures. If these networks are to continue to prosper in this changed competitive environment, and fulfill their traditional role as providers of first-quality programming for free over-the-air television, they must have reasonable freedom to contract for the ensured distribution of that programming -- freedom their subscription multichannel rivals already enjoy, without limitation of any kind.

The increased competition facing the three original networks is extensively documented. As the Commission recently noted in repealing the prime time access rule, the audience shares of the three original networks have dropped precipitously as a result of competition for viewers. Focusing for purposes of that proceeding on prime time alone, "the time period when the networks' viewing shares are the highest," the Commission found that "each network's average share of the prime time audience declined from a 31.1 viewing share

³⁸ At least as long ago as 1989, the Commission, in its report abolishing the two-year limitation on network-affiliate agreements, implicitly adopted the networks' view that "[n]umerous sources of non-network programming are now available to stations, making affiliation but one option among many available means of obtaining programming." Review of Rules and Policies Concerning Network Broadcasting By Television: Elimination or Modification of Section 73.658(c) of the Commission's Rules, 4 FCC Rcd 2755, 2756 (1989) ("Two-Year Affiliation Rule Report and Order").

during the 1971/72 season to a 20.2 share during the 1993/94 season, a loss of almost one-third of each network's audience."³⁹

The networks similarly have suffered a significant decline in their shares of national advertising revenues. As the Commission found in the PTAR proceeding, if national advertising revenues are considered without regard to national spot sales, by 1993 the average shares of the three original networks had dropped to less than 23 percent each.⁴⁰ This figure represents a loss by each network of approximately a third of its national advertising revenue share from 1979, when the networks still cumulatively earned 100 percent of national television advertising revenues.⁴¹ The decline in networks' national advertising share is attributable to the

³⁹ PTAR Report and Order at ¶29, citing PTAR Joint Economic Study at 18-19. Inclusion of dayparts outside of prime time provide a more complete measure of the reduced size of the networks' audience share. In November 1994, the total day share of audience for the three networks' affiliates together had fallen to 47.5 percent, with the remaining 52.5 percent captured by independents and Fox affiliates (17.9 percent), PBS (3.6 percent), basic cable (27.7 percent) and pay cable (3.6 percent). Nielsen Television Index Special Analysis (October 31, 1994 - November 27, 1994). The average total-day audience share for each of the three networks' affiliates attributable to dayparts programmed by the networks has dropped from 17 during the 1980/81 season to 12 during the 1993/94 season. PTAR Joint Economic Study at 19 and Appendix A, Table A-9.

⁴⁰ PTAR Report and Order at ¶37, citing PTAR Joint Economic Study at 20 and Appendix A, Table A-10. If national spot sales are considered, as we believe they must be, see Comments of CBS Inc., In re Review of Regulations Governing Television Broadcasting, MM Docket Nos. 91-221 and 87-8 (May 17, 1995) at 30-32 ("CBS Multiple Ownership Comments") and Comments of CBS Inc., In re Review of Regulations Governing Broadcast Television Advertising, MM. Docket No. 95-90 (August 28, 1995) at 9 and n.16, the three traditional networks' share of national video advertising is only 14.6 percent. PTAR Joint Economic Study at 20.

⁴¹ PTAR Joint Economic Study at 20 and Appendix A, Table A-10.

rapid growth of competitors to the networks, particularly national cable networks and syndicators of nationally-exhibited programming.⁴² As the Commission staff observed in 1991,

At least since 1980, the network share [of advertising revenues] has dropped continuously and substantially. ... While the components of video advertising are all predicted to grow, the rates of increase are expected to vary greatly, with the cable and national syndication categories gaining in share at the expense of the others.⁴³

Competition from cable networks, first-run syndicators, and other alternative television services are realities to which the broadcast network must adjust. However, if they are to compete as purveyors of first-quality programming against dual revenue stream providers,⁴⁴

⁴² From 1983 to 1988, national advertising revenues for syndication and for cable more than tripled. See Notice of Proposed Rulemaking in MM Docket No. 95-90, FCC 95-226 (released June 14, 1995) at Appendix A. From 1988 to 1993, syndication advertising revenues increased by 74.9% and national cable advertising revenues more than doubled, while the combined advertising revenues of the broadcast networks increased by only 11.3 percent -- even though the revenues of a fourth network (Fox) were added during this period. Id.

⁴³ OPP Report, 6 FCC Rcd 3996 at 4071

⁴⁴ The Commission's Office of Plans and Policy concluded in 1991 that the capacity of cable to generate revenue on a per viewer-hour basis had already substantially outstripped that of broadcasting:

Including cable network and local cable operator advertising, cable industry revenues were 71.8 percent as great as those of the broadcast industry, or 41.8 percent of the broadcast-cable total. Yet cable, including distant signals and superstations, accounted for only 32 percent of viewing in 1989/90 and cable advertising remains far below its potential level. Clearly cable has succeeded in earning much more revenue per viewer-hour than broadcasting.

OPP Report, 6 FCC Rcd. at 4048, citing Cable Television Advertising Bureau, Cable TV Facts, 1990 ed., 12-13.

broadcast networks must be permitted to maximize the efficiency of their distribution.⁴⁵ Regulations that artificially reduce the networks' ability to bargain for clearance of their programs undermine the viability of broadcast networks and promote the shift of first-quality programming from free television to cable. Affiliate preemptions of network programming not only reduce the size of the audience exposure the advertiser is purchasing, but also reduce the extra value of full simultaneous network exposure, which is important to advertising campaigns linked to particular events or promotions. This, in turn, undermines the capacity of broadcast networks to support the production of expensive first-quality programming through advertising revenues alone.

All of this is not to say, of course, that affiliates should have no right to preempt network programming. As licensees obligated to serve the needs of their communities, the operators of affiliated stations must retain the right to reject network offerings which they genuinely believe to be unsuitable or contrary to the public interest. Moreover, affiliates should

⁴⁵ In repealing the two year limitation on affiliation agreements, the Commission has previously recognized the importance of eliminating restrictions on network-affiliate relations that handicap networks vis-a-vis their nonbroadcast competitors:

[I]t is critical that regulations, like the "two-year" rule, not adversely distort the competitive interplay between broadcast networks (and their affiliates) and the newer cable networks (and their affiliates). The broadcast networks and their affiliates now face, and will increasingly face in the future, the need to compete aggressively both for programming and for viewers with nonbroadcast networks.

Two-Year Affiliation Rule Report and Order, 4 FCC Rcd at 2757. The Commission concluded that elimination of the two-year limitation would be of assistance to networks in planning programming schedules, attracting advertisers and attracting capital. *Id.* Elimination of restrictions hampering networks' ability to negotiate for fuller clearances of their programs would provide even greater assistance in these respects.

clearly continue to retain the discretion to preempt network programming to present news and public affairs broadcasts, as well as other public-service programs, which they deem to be of greater local or national importance. Indeed, the CBS Owned television stations themselves preempt network programs in order to air local broadcasts of this kind.

As shown below, however, most affiliate decisions to preempt network programming are economically driven. It is with respect to these preemptions that we believe networks must have the freedom to negotiate fuller clearances. For the reasons discussed above, affiliated stations will not be without bargaining power to seek maximum flexibility in determining whether to preempt network programs, or, alternatively, to demand increased levels of compensation in exchange for agreed limitations on that discretion. The point, however, is that broadcast networks must have comparable ability to that of their competitors -- such as cable networks and syndicators -- to negotiate for the ensured distribution of their product which is necessary to support high quality programming. Given the emergence of new networks and the growing strength both of network affiliates and independent stations, there is little reason to retain government regulations which unduly restrict the ability of networks and affiliates to reach their own bargains in this regard.

II. The Repeal Or Substantial Modification Of Network/Affiliate Rules That Create Marketplace Distortions Is Necessary To Promote The Continued Viability Of Universal Free Network Broadcasting, And Will Not Inhibit The Development Of New Networks Or Interfere With Stations' Fulfillment Of Their Public Interest Obligations.

A. The Right To Reject Rule

The capacity for advertising revenue alone to support expensive first-run television programming is largely a function of the size of the audience to which that

programming is exposed. It is for that reason that the national broadcast television networks are so important to the maintenance of universal free access to first-quality television programming. It is these networks that offer by far the most efficient method of exposing programs to the widest possible audiences, thus maximizing advertising support for the programs.⁴⁶

With the fragmentation of audience brought on by the proliferation of alternative television services, the ability of the national broadcast networks to attract the audience levels necessary to support first-quality programming has become critical. In its Notice in this proceeding, the Commission expressly recognizes that affiliate preemptions can have the effect of undermining the ability of broadcast networks to attract such audiences. Thus the Notice states:

Ensuring an affiliate an unlimited right to reject programming provided by a network enables an affiliate to pursue its short-term interests to the possible detriment of the network system within which it participates. ... Losses in network advertising revenues imposed by affiliate preemption affect the network's ability to fund popular new programming and thus affects the future profitability of the network and all the affiliates. Further, such behavior by stations may induce networks to avoid innovative programming, because the network would bear most of the risk

⁴⁶ As the Network Inquiry Staff observed:

More resources can be expended on program production if those costs are spread over a large number of outlets and viewers. More funding for a national distribution system can be achieved if a national market in the sale of commercial time is established. Television networks are not profit-siphoning intruders into a system of local broadcast stations; they are indispensable organizers of the nation-wide system of television broadcasting.

Network Inquiry Report at 519-20.

of airing such programming with affiliates sharing in the benefits only when it serves their interests.⁴⁷

Accordingly, the Commission proposes to retain the right to reject rule⁴⁸ to the extent that it allows affiliates to preempt network programming based on public interest considerations, while clarifying that the rule may not be invoked solely for financial reasons.⁴⁹ CBS strongly supports this proposed clarification. Indeed, a contrary interpretation of the rule, which would preclude networks from bargaining with affiliates to prevent economically-based preemptions of their programming, would serve no public interest. Rather, it would simply have the effect of allowing affiliates to enjoy greater financial benefits from the network-affiliate relationship than they would otherwise have been able to negotiate -- a result which clearly should not be dictated by government regulation.

⁴⁷ Notice at ¶22.

⁴⁸ The rule states that:

No license shall be granted to a television broadcast station having any contract, arrangement, or understanding, express or implied, with a network organization which, with respect to programs offered or already contracted for, pursuant to an affiliation contract, prevents, or hinders the station from (1) rejecting or refusing network programs which the station reasonably believes to be unsatisfactory or unsuitable, or contrary to the public interest, or (2) substituting a program which, in the station's opinion, is of greater local or national importance.

47 C.F.R. §658(e).

⁴⁹ As the Commission notes, it is presently unclear whether the right to reject rule allows a station to preempt network programming for purely economic reasons. Notice at ¶24. At the least, there is a strong argument based on the language of the rule that it affords affiliates a right to preempt network programming only on the basis of bona fide public interest considerations, rather than for reasons of financial gain.